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PNC

March 26, 2007

VIA E-MAIL

Nancy C. Morris, Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549-1090
Rule-Comments@sec.gov

Jennifer J. Johnson, Secretary
Board of Governors of the
Federal Reserve System
20th Street & Constitution Ave., N.W.
Washington, DC 20551
Regs.comments@federalreserve.gov

Re: Definitions of Terms and Exemptions Relating to the "Broker" Exceptions for Banks; File No. S7-22-06; Docket No. R-1274; Federal Register 77522 (Dec. 26, 2006)

Dear Ms. Morris and Ms. Johnson:

The PNC Financial Services Group, Inc. ("PNC"), Pittsburgh, Pennsylvania, appreciates the opportunity to comment on the proposed Regulation R jointly issued by the Securities and Exchange Commission (Commission) and the Board of Governors of the Federal Reserve System (Board), (hereinafter collectively referred to as "Agencies"), to implement certain exceptions for banks from the definition of the term "broker" under Section 3(a)(4) of the Securities Exchange Act of 1934 ("Exchange Act"), as amended by the Gramm-Leach-Bliley Act ("GLBA").

PNC is one of the largest diversified financial services companies in the United States, with $101.9 billion in assets as of December 31, 2006. PNC engages in retail banking, institutional banking, asset management and global fund processing services. Its principal subsidiary bank, PNC Bank, National Association ("PNC Bank"), Pittsburgh, Pennsylvania, has branches in the District of Columbia, Florida, Indiana, Kentucky, Maryland, New Jersey, Ohio, Pennsylvania and Virginia. PNC also has 12 other subsidiary banks, which are located, and have branches in, Maryland, Virginia and Delaware.

PNC also has several broker-dealer affiliates, including J.J.B. Hilliard, W.L. Lyons, Inc., which is a member of the National Association of Securities Dealers ("NASD") and the New York Stock Exchange; and PNC Investments, LLC, PNC Capital Markets, Inc., and Mercantile Brokerage Services, Inc., which are members of the NASD. PNC also offers investment management, custody and fiduciary (including trust) services through departments of PNC Bank, National Association, PNC Bank, Delaware, Mercantile-Safe Deposit and Trust Company, Baltimore, Maryland, and Mercantile Peninsula Bank, Selbyville, Delaware, which are regularly examined by bank examiners for compliance with fiduciary principles and standards.

As you well know, the trip from Regulation B to Regulation R has not been without its pitfalls, and we appreciate the hard work by the leadership and staff at both Agencies in formulating and issuing this new proposal. Our original comment letter on Regulation B focused on our view that the regulation did not reflect Congressional intent and would restrict the ability of banking organizations to continue activities in which they had engaged without notable problems for years. By contrast, the current proposed regulations generally incorporate the intent of Congress, and the comments address particular issues raised by the proposed regulations. We join the other commenters in commending the Agencies on this much improved proposal.

PNC participated actively in the formulation of the comment submitted by the American Bankers Association ("ABA") and its affiliate the ABA Securities Association ("ABASA"), and strongly endorses the ABA/ABASA comment letter. Rather than repeat all of the recommendations set forth in that letter, we are focusing on those issues that are of particular concern to PNC.

PRELIMINARY MATTERS

The Need for Legal Certainty Regarding Dual Bank Broker-Dealer Employees

We join in the request of the ABA/ABASA to resolve the issues of dual bank broker-dealer employees and their request for a clarification of the applicability or not of the NASD's Rule 3040.

Applicability of Multiple GLBA Exceptions

We request confirmation of the informal advice given previously by the staff of the Agencies that the statutory exceptions and the proposed exemptions in Regulation R are not mutually exclusive, and that activities that are excepted or exempted under one provision may also be excepted or exempted under another provision of the Exchange Act, GLBA or Regulation R and that a bank may choose with which of the applicable exceptions or exemptions it will comply for specific activities.

Future Regulatory Action

We join the ABA/ABASA in supporting continued joint rulemaking and the issuance of joint guidance by the Commission and the Board and consultation with the other bank regulators and we request that the Board and the Commission reach some common understanding that they will consult each other in connection with the institution of any enforcement actions, including administrative cease and desist orders, involving GLBA and related regulatory issues, particularly when such action may involve new interpretations.[1]

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[1] See the ABA/ABASA letter for a discussion of Dunham Trust Company. *See also* www.sec.gov/litigation/admin/2006/33-8740.pdf.

DISCUSSION OF REGULATION R

1. NETWORKING EXCEPTION

A. Referral Fees

GLBA provides that unregistered bank employees may receive compensation for the referral of customers to broker-dealer firms if the compensation is "a nominal one-time cash fee of a fixed dollar amount and the payment of the fee is not contingent on whether the referral results in a [brokerage] transaction." Proposed Rule 700 alternatively defines the statutory term "nominal one-time cash fee of a fixed dollar amount," in terms of either multiples of base hourly wages or fractions of annual base salaries for the referring employee's job family, twice the employee's actual base hourly wage, or $25. Moreover, the proposal provides that the flat $25 referral fee could be adjusted for inflation.

However, personnel such as mortgage brokers, syndicated lenders, private bankers and trust sales persons may receive relatively low base salaries together with high contingent compensation. Therefore, we request that the proposal be revised to permit another alternative measure of "nominal one-time cash fee" based on total hourly or annual compensation for the referring employee, so long as that portion of the individual's compensation that is based on securities transaction referrals is not included in total hourly or annual compensation. Under this formulation, bank employees could be paid a nominal referral fee that is twice their total hourly wage or 1/1000th of their total annual compensation consisting of their base salary and non-securities contingent compensation paid.

The definition of "referral" provides that a bank employee must direct a bank customer to the broker-dealer partner. We would suggest that referral also encompass potential customers. It is not uncommon for a potential customer seeking financial services to approach the bank. After discerning the particular needs of the potential customer, the bank employee may refer the potential customer to its broker-dealer partner. The bank employee should be compensated for that referral despite the fact that the party referred was not a bank customer.

B. Bonus Plans

While we continue to maintain that Congress, in enacting the networking exception in GLBA, intended only to prohibit the payment of traditional brokerage commissions, not bonuses, to bank employees, we are pleased that the Agencies have defined the term "incentive compensation" in such a manner that it should not restrict traditional bonus plans. Specifically, proposed Rule 700(b)(1) would permit bonus plans that are paid on a discretionary basis and are based on multiple factors and variables that include significant factors and variables that are not related to securities transactions at the broker-dealer, and do not include securities referrals as a factor or variable in setting the employee's compensation. Consequently, balanced, discretionary bonus plans that measure the revenue generated by, or the profitability of, a total customer relationship would satisfy the Rule's requirements because the plan would include significant

factors and variables that are not related to securities transactions. This would be true despite the fact that the bonus plan would include significant factors and variables that are securities related, such as revenues derived from securities underwriting and brokerage services provided by the broker-dealer that may have been initially generated by a bank employee referral.

Proposed Rule 700(b)(2) makes clear that bonus plans may also take into account the financial performance of the bank, bank holding company, a bank holding company affiliate or operating unit, or, under certain circumstances, a broker-dealer. We encourage the Agencies to allow bonuses to be paid to individuals based on the financial performance of a branch, division, or geographic or operational unit of a broker-dealer. Non-bank affiliated brokerage firms do so, and we see no reason why broker-dealers affiliated with banks should not have the same flexibility to share operating unit profits with their employees.

C. Institutional Referral Exemption

Proposed Rule 701 would allow banks that meet all the other conditions of the networking exception to pay referral fees that need not be nominal in amount to bank employees for referring high net worth or institutional customers to a broker-dealer. These referral fees also may be contingent on the consummation of a sale. However, the proposed rule itself is very proscriptive and burdensome.

(1) High Net Worth and Institutional Customer Definitions

We believe that the proposed financial tests for high net worth and institutional customers are unnecessarily high and make an unnecessary distinction between natural persons and legal entities. For example, for the purpose of determining which referred persons are capable of understanding the arrangements involved in a compensated referral to a broker-dealer, we believe that investor protection would be served by relying upon the definition of "accredited investor" found in Rule 501 of Regulation D promulgated under the Securities Act of 1933, as amended. Among other things, use of the "accredited investor" definition would accord traditional treatment to spouses with jointly owned assets, rather than limiting each spouse to counting only 50% of jointly owned assets, and would not require that an inter vivos or "living trust" be treated in the same manner as a business corporation when, we would submit, it should be qualified on the basis of the settlor's net worth.

(2) Other Procedural Requirements

It is our understanding that bank employee referrals of current and prospective customers encountered in the ordinary course of an employee performing his or her assigned duties, includes the performance of those duties beyond the four walls of the banking institution, such as at civic, sporting and social functions. Such referrals that satisfied the other conditions of proposed Rule 701 would qualify for the payment of enhanced fees.

Proposed Rule 701(a)(3) mandates that a written agreement between the bank and the broker-dealer provide, among things, that the bank and the broker-dealer determine that the referring bank employee is not subject to statutory disqualification under the Exchange Act. We do not think that both entities need incur the time and expense to perform this analysis. Because of the technical complexities associated with determining whether a person is statutorily disqualified, it would be more appropriate for the responsibility for making this determination to be negotiated between the broker-dealer and the bank according to which entity is best suited to perform the analysis. Similarly, we believe that the bank and the broker-dealer may determine who would qualify the customer and when; provided that the qualification took place no later than the time the referral fee was paid to the bank employee. A broker-dealer performing its "know your customer" and, if applicable under self-regulatory rules, suitability, responsibilities would be able to determine that the customer is qualified as a high net worth investor at the time the broker-dealer effects the securities transaction on the customer's behalf but before any referral fee is paid to the bank employee.

We strongly object to the requirement that the broker-dealer must perform a suitability analysis regarding the securities transaction at issue. Suitability analyses should only be required in accordance with the rules of the self-regulatory organizations (SROs) and those rules do not require performance of suitability analyses on unsolicited transactions. Yet, this proposal would require the broker-dealer to do just that.

2. TRUST AND FIDUCIARY EXCEPTION

Under GLBA, a bank can effect securities transactions in connection with providing trust or fiduciary services and remain exempt from registration as a broker as long as four basic conditions are satisfied. First, the bank cannot publicly solicit brokerage business, other than by advertising that it effects transactions in securities as part of its overall advertising of its general trust business. Second, the bank's compensation for effecting transactions in securities must consist chiefly of an administration or annual fee; a percentage of assets under management; a flat or capped per order processing fee that does not exceed the cost of executing the securities transaction for trust or fiduciary customers, or a combination of such fees. Third, the bank would have to direct all trades of publicly traded domestic securities to a registered broker-dealer. And fourth, the bank must effect the transactions in a department that is regularly examined by bank examiners for compliance with fiduciary principles and standards.

The purpose of this exception is to continue to allow banks to engage in the types of trust and fiduciary activities they have engaged in for many years, even if a substantial portion of those activities generate fees that would otherwise trigger broker registration requirements. In providing this exception, Congress recognized that where banks conduct securities transactions in their fiduciary capacity, they are subject to an entirely separate scheme of bank fiduciary regulation.

We are pleased that the Agencies' proposal has taken several steps to significantly reduce the burdens and expenses associated with complying with the trust and fiduciary exception's "chiefly compensated" requirement. Of particular note is the fact that the Agencies now propose in Rule 721 to include fees permitted by Rule 12b-1 of the Investment Company Act and other types of fees paid by investment companies and their service providers within the meaning of fees based on assets under management, and therefore permitted by GLBA. And while we continue to question whether GLBA actually requires banks to calculate "chiefly compensated" on an account-by-account basis, we are pleased that the Agencies have provided what appears to be a workable bank-wide exemption that will not require banks to perform an account-by-account analysis of its compensation.

We do have the following comments to make with respect to the definitional provisions of proposed Rule 721 and the bank-wide exemption requirements of proposed Rule 722.

A. Relationship Compensation

It is our understanding that, under proposed Rule 721, included within the definition of "relationship compensation" are the fees received from investment company complexes for the types of services listed in the proposed rule, whether such fees are paid by the investment company itself or by any of the investment company's service providers, such as its administrator, primary distributor, investment adviser, or transfer agent. This interpretation is supported by the narrative portion of the release as well as the text of Rule 721 itself. We would, however, recommend that the applicable provisions of proposed Rule 721 be revised to clarify that the fees may be paid by an investment company or any such service provider.

The definition of relationship compensation should cover certain other fees as well, if earned in accounts for which the bank is relying on the trust and fiduciary exception, such as fees earned in connection with securities lending activities. With respect to securities lending activities, banks generally share, with their trust and fiduciary clients, the income earned on reinvestment of the cash collateral posted by the securities borrower as part of the lending compensation arrangement. We note that the list of fees qualifying as "assets under management" is "without limitation" and believe that the portion of the income or compensation earned on the cash collateral associated with securities lending transactions could properly be classified as an "assets under management" fee for accounts for which the bank is relying on the trust and fiduciary exception.

We also believe that performance-based fees should be considered assets under management fees. By measuring the growth of assets under management during a given period relative to some standard benchmark or measure of the market, such as the S&P 500 Index, these types of fees are, in essence another variation of a fee imposed on assets under management. At no time does the number of transactions affect the fee and, in fact, the investments could remain static throughout the year and still beat a standard measure of market performance.

Settlement fees are fees that may be earned in directed trust accounts on trades placed with a broker-dealer by an outside investment manager. These fees are assessed for the administrative services necessary to settle the transaction, not to execute the transaction which has already been performed by the broker-dealer. While these fees are frequently set as a flat per order processing fee, they should be distinguished from the statutory limits placed on flat per order processing fees associated with executing securities transactions. We believe that this fee should be properly characterized as an administrative fee. We would note that settlement fees are permissible under the custodial exception, as well as proposed order-taking exemption. We also believe that disbursement fees, wire transfer fees and other similar types of fees should also be classified as administrative fees, and, therefore, relationship compensation.

B. Two-Year Rolling Average

We understand that calculation of "chiefly compensated," whether performed on an account-by-account basis or on a bank-wide basis, requires averaging the percentages obtained for each of the two immediately preceding years. We further understand that compliance with proposed Regulation R will not be required until the first fiscal year beginning after June 30, 2008 and, thus, for those banks whose fiscal year coincides with the calendar year, compliance will not be required until January 1, 2009. Once compliance is required, only then will a bank be required to start collecting the requisite data to perform the two-year rolling average calculation.

This calculation should only be required to be performed once a year, not on a rolling basis, and the yearly calculation would be performed within a reasonable time after the relevant information necessary for the calculation had become available. So that the requisite systems can be developed in a timely and least burdensome manner, we request confirmation of our understanding.

C. Other

We request that the Agencies give flexibility to banking organizations to calculate their relationship to total compensation ratios either on a bank-wide basis, as currently contemplated under proposed Rule 722, or on a bank holding company basis. An organization that has more than one banking institution subsidiary may wish to perform this calculation on an enterprise-wide basis.

3. SAFEKEEPING AND CUSTODY EXCEPTION

GLBA excepts from broker registration various activities conducted by banks in connection with safekeeping and custody services long provided by banks as part of their customary banking activities. Proposed Rule 760 would allow banks, subject to certain conditions, to accept orders for securities transactions from custodial customers. We continue to question the need for this exemption as Congress clearly contemplated providing banks, under GLBA, with the ability to continue to provide order-taking services for custodial clients.

We note that the narrative portion of the release makes quite clear that a bank that is engaged in non-order taking custodial services need not rely on the exemption provided by proposed Rule 760. These services are excepted under the statute itself.

The proposal distinguishes order-taking services provided to employee benefit plans and similar accounts from order-taking services provided as an accommodation to all other custodial clients. More restrictive conditions attach to the latter.

A. Employee Benefit Plans, Individual Retirement and Similar Accounts

Congress frequently revises the provisions of the Internal Revenue Code governing tax-favored savings accounts. Accordingly, we request that a provision allowing for new types of plans to be treated as employee benefit plans under the rule be added to Rule 760. In addition, we suggest that banks be able to provide order-taking services for escrow, paying and disbursement agency accounts and that the less restrictive conditions of proposed Rule 760(a) attach to these accounts.

Further, a bank providing custodial services to an affiliated or non-affiliated trust company or bank trust department should be able to provide order-taking services to those institutions under the same conditions as banks that serve as custodians to employee benefit plans and similar accounts. In both situations, a fiduciary is interposed between the beneficial owner and the custodial bank, thereby reducing the need for the additional restrictions associated with accommodation orders. In those situations, where a bank serves as custodian for a bank trust department or trust company, there is no need for the more restrictive conditions associated with accommodation trades as it is the fiduciary organization, not the individual investor, that is placing the order.

The employee compensation restrictions do not prohibit a bank employee from receiving compensation that recognizes the employee for his efforts in selling the bank's custodial services, as well as bonuses and referrals permitted under proposed Rules 700 and 701. The exemption also properly recognizes that some banks function as non-fiduciary and non-custodial administrators and recordkeepers for employee benefit plans and provides for an exemption for these banks.

B. Accommodation Orders

For all non-employee benefit plan and tax-favored accounts, proposed Rule 760(b) would exempt from broker registration any bank that accepts securities orders for custodial accounts only as an accommodation to that customer, subject to the restrictions discussed below.

The proposal would place restrictions on the fees banks could earn for providing order-taking services. Appropriately, the bank fee restrictions do not restrict a bank from charging the

client a fee for providing the order-taking service that varies based on the type of security purchased or sold.

In addition, the proposal limits the ability of banks to provide investment advice or research to, or make recommendations to, or solicit securities transactions from the account, while allowing banks to cross-market investment management services, including sharing examples of investment research prepared by the trust department for trust and fiduciary customers. Moreover, providing custodial customers with an array of investments, e.g., mutual funds, from which to choose from would not constitute investment advice or recommendations.

C. Carrying Broker Activities

GLBA's safekeeping and custody exception does not apply if "the bank, in connection with such activities, acts in the United States as a carrying broker (as such term, and different formulations thereof, are used in section 15(c)(3) of [the Exchange Act] and the rules and regulations thereunder) for any broker or dealer, unless such carrying broker activities are engaged in with respect to government securities." Proposed Regulation R does not address the meaning of the term "carrying broker" for the purposes of this provision. We request that the Agencies commit in the Final Rule not to adopt or adhere to any separate or joint interpretation of GLBA's "carrying broker" provision, until and unless they jointly issue notice, and provide an opportunity to comment, on a proposed joint interpretation.

4. SECURITIES LENDING EXEMPTION

Proposed Rule 772 provides an exemption for securities lending services when the bank is not also performing custodial services for the customer. We would strongly encourage the Agencies to affirm explicitly in the final rule's preamble that the requirements under the exemption for securities lending activities conducted as agent in the non-custodial context do not apply to the securities lending activities of custodians.

5. BROKER-DEALER EXECUTION

To qualify for the trust and fiduciary and custody exemptions, GLBA requires trades conducted under these exemptions to be directed to a registered broker-dealer for execution. However, because securities of most mutual funds are neither traded on a national securities exchange nor through the facilities of a national securities association or an interdealer quotation system, Rule 775 permits these trades to be effected either through the National Securities Clearing Corporation's Mutual Fund Services (NSCC) or directly through the mutual fund's transfer agent, provided that: (1) the shares are distributed by a registered broker-dealer, and (2) the sales charge is limited to what the broker-dealer could charge under applicable regulations.

We note that the purchase and sale of variable insurance products, such as variable annuities, that are held in insurance company separate accounts is also not accomplished through registered broker-dealers and is often accomplished directly with the issuing insurance company. In such situations, it is the insurance company that maintains policy holder records, acting, in effect, as the transfer agent for the variable insurance products it issues. Alternatively, settlement may be accomplished through settlement services offered by NSCC to insurance companies. We recommend that the agencies expand the scope of Rule 775 to include variable insurance products.

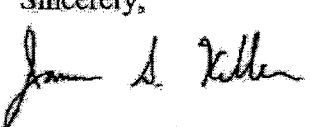
6. MONEY MARKET MUTUAL FUND EXEMPTION

We support the Agencies' proposal to exempt banks effecting transactions in money market mutual funds from broker registration.

Conclusion

Thank you again for providing this opportunity to comment. While we have commented on particular facets of the proposal, we would like to reiterate that we are fully supportive of the comment letter submitted by the ABA/ABASA. If you have questions about this comment letter, please feel free to contact me.

Sincerely,



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